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Bank Examinations by Public Accountants

BY FREDERICK MARTIN
(Philadelphia Office)

One of the best statements ever made on the subject of this paper was made by Mr. George V. McLaughlin in an address delivered a few years ago before the New York State Society of Certified Public Accountants. No one could be better qualified than Mr. McLaughlin to make such a statement for he has had experience from almost every angle of the situation. He is a certified public accountant, he has been Superintendent of Banks of the State of New York, and for quite a number of years he has been president and a member of the board of directors of the Brooklyn Trust Company.

In expressing his conviction as to the vital need for private examinations of banks by independent accountants, he outlined what seemed to him the cardinal points of the subject as follows:*

I. Recent Increase in Number of Bank Examinations

- (a) Due largely to requirements of public authorities—FDIC and RFC now have right to examine.

- (b) Many banks now examined six times a year.

II. Private Examinations, Nevertheless, More Important Than Ever Before

- (a) Bank directors now take their responsibilities more seriously. Their need for information, therefore, is greater.

- 1. During prosperous times, banks seem to run themselves; directorships then are often considered mostly honorary.
- 2. Recent events and laws have changed the attitude of directors to one of great caution.

- (b) Physical impossibility of directors of large institution to make examination themselves.

- 1. Directors have neither time nor technical training necessary to do it.
- 2. Impossible for directors to digest mass of new law and regulations governing banking because they are usually engaged in some other business.

- (c) It is a mistake for directors of small institutions to attempt to make their own examinations.

* Reproduced in *The New York Certified Public Accountant* of January, 1935.

1. Independent viewpoint needed.
2. Technical knowledge of accountant needed, no matter how small the bank may be.

III. Private Examinations Should Cover All Activities of the Bank

- (a) Trust department, when there is one, should be examined in order that directors' information may be complete.

IV. While Directors are Entitled to All Possible Information, General Public is Not

- (a) Business of banks is by nature personal and confidential, as contrasted with impersonal nature of business done by industrial and public utility companies.
- (b) Publication of contents of a report covering the examination of a bank is likely to embarrass customers.

V. Condensed Statement of Condition Intelligible to Layman is Ideal

- (a) Canadian bank statements longer than ours, but furnish no more information, and are less understandable.
- (b) Too much detailed information in bank statements may encourage "window dressing."

VI. Fewer and More Thorough Bank Examinations Should Be Our Goal

- (a) Coordination of examinations to eliminate duplication and waste motion should be brought about.
- (b) Too many examinations leads to competition in stringency between examiners—each group is afraid they will overlook something which the next group will criticize.

- (c) The time for stringent examinations is during prosperity, when most of the mistakes are made—not during depression.
- (d) To make an ideal examination, the examiner should not permit his judgment to be swayed by public sentiment or prevailing psychology.

DIRECTORS' EXAMINATIONS

The Comptroller of the Currency of the United States and many state banking codes make it obligatory for directors to examine the assets and accounts of banking institutions, but permit the directors to delegate this duty to, or secure the aid of, others. In some states, banking codes require that a copy of the report upon each examination be forwarded to the state banking department. In complying with these requirements the services of public accountants are frequently employed for the reasons stated above. In other cases accountants are employed because the directors are aware of their limitations.

In the case of large institutions, it is a physical impossibility for the directors or other officials to make the examination, because they usually do not possess the necessary technical training, and since most of the directors are engaged in other lines of business, they are not intimately acquainted with the mass of new laws and regulations governing banking. Directors of small institutions also do not have the technical training necessary to make an examination, and they lack one of the chief at-

tributes of the public accountant, namely, an independent viewpoint.

In a pamphlet issued by the Comptroller of the Currency several years ago he emphasized the obligation of bank directors to avoid permitting examinations to become routine or perfunctory, and went on to say, "an examination twice a year by a committee of directors, or by accountants at the instance of the board, who will give sufficient time to the work to make it thorough and complete, cannot fail to be of great benefit to all concerned, and this the directors owe to the shareholders who have placed them in positions of trust."

SAVINGS BANKS EXAMINATIONS

This is as true in the case of savings banks as it is in the case of commercial banks—perhaps even more so. Because these banks are mutual, and the public, represented by the depositors, holds the entire stake, each trustee should be fully aware of his responsibility and should be fully informed by someone independent of the management if he is to administer faithfully and efficiently the trust imposed upon him when he accepted his appointment.

Relatively few savings banks have availed themselves of the services of independent accountants, but their number is increasing as trustees, awake to their responsibility, insist on a review of the bank's affairs by representatives of their own choosing.

PUBLIC ACCOUNTANTS' WORK

It is well known that, depending upon the size of the institution, many men are necessary to make the examination as expeditiously as possible. The financial institutions must be examined in the shortest possible time in order not to interfere with current business and it requires considerable technical knowledge on the part of the examiners, not only as to the transactions, but also as to the procedure of audit. The balance of this paper will attempt to portray the principal procedures employed in the examination of a commercial bank which also maintains a trust department.

At the outset it is well to emphasize that examinations of the majority of banking institutions are what is generally known as balance sheet examinations in which the asset and liability accounts at the balance sheet date—that is the financial position of the bank—are confirmed or tested to the extent considered adequate. In such an examination the details of the income and expense accounts during the fiscal period ending with the balance sheet date are examined to a limited extent only and, consequently, there is no absolute assurance that all errors in these accounts will be discovered. Nevertheless, such an examination, unless modified by the desires of the directors of the bank, is sufficient for all practical purposes and ordinarily it is not considered necessary to verify all of the transactions.

The public accountant engaged to examine the financial statement of a bank should make every effort to plan the engagement well in advance of the examination date. He should, if feasible, ascertain the general layout of the banking space, position of the vaults, number of tellers, etc., so that the examiners will enter the bank with a definite plan in mind and each of the examiners will know where he is to go and what he is to do. The sequence of procedures is also important and, while it depends on the type of bank being examined, fundamentally it does not vary on any engagement.

Ordinarily, the first consideration after the general planning of the engagement has been completed, will be the assignment of the men to their locations and the instructions that each man is to receive. Consideration should also be given to the assigning of men to seal all reserve cash funds which are not to be counted immediately, and to seal files, safes and other depositaries containing items which are not given early attention. The exchange rack and vault should be placed immediately in charge of an examiner, and various books and records placed under control.

The examiner in charge should review the accounting procedure, the system of internal control, and the scope of work done by the bank's own auditors. The amount of detail work to be done on the examination will depend in some measure on the

adequacy or inadequacy of such system and procedure.

All the accountants on the engagement should be instructed to observe carefully the accounting procedure and the system of internal control; if any deficiencies are noted, they should be reported to the examiner in charge. Accounting systems used by banking institutions are often formulated by various members of the organization; consequently banking systems are not always planned and installed by those having adequate knowledge of systems.

For convenience the procedure which, in my opinion, should be followed in an examination of the various items on the balance sheet will be discussed in the order in which they ordinarily appear on the statement. However, the order of the work depends to a great extent on the number of accountants making the examination and the necessity for the prompt release of the assets and records.

Assets

CASH AND CASH ITEMS

The tellers' and vault cash should be verified by count. Large bills should be counted in their entirety and the packages of small bills (one's, two's and five's) tested by counting a reasonable portion of them. Although it should not be necessary to open all packages and bags of coin, the accountant should be satisfied that they contain the amounts indicated on the tags. As a matter

of practical procedure, it is better to make a bulk count of each teller's cash and the vault cash before counting the individual bills in bundles, for by so doing, a tally may be obtained for comparison with the tellers' proofs more quickly, after which the bundles may be proven. Needless to say, each teller's cash must be controlled to avoid the possibility of counting the same cash twice.

All "cash items" should be listed in detail showing dates of checks, makers, drawees, payees, latest endorsers and the reasons for holding. Coupons should be listed, showing due dates, the names of customers having deposited or cashed them, and the reasons for holding. Any debit memoranda carried as cash should be described fully, including the dates and the names of the officers approving the charges. In addition to submitting the schedules of cash items to the officer in charge for his approval, the subsequent collection of the items must be traced through the records.

Exchanges for the clearing house should be gone into to ascertain that they are regular. Requests for confirmation of payment and the correctness of the totals of the items sent to the various member banks should be enclosed with the clearings, and control maintained until delivered to the clearing house. The requests for confirmation should provide space for the listing of any items returned and the reasons therefor. As the returned items will be received by

the bank before the accountant receives the confirmations, the teller to whom returned items are presented should be notified to submit all such items to the accountant for inspection, in order that the charging of them to depositors from whom they were received, or subsequent collection thereof, may be traced.

If the examination is begun in the afternoon, the outgoing transit letters should be examined and confirmation requested from the collecting banks of the correctness of the totals of the letters and details of any "mis-sorts." The incoming mail should be examined, regardless of the time of commencing the examination, until sufficient time has elapsed for the return of uncollected items included in the outgoing mail on the examination date. Items returned which were sent out on the examination date should be listed and their collection traced, and a comparison of the totals of the return item letters should be made with the charges on the bank statements when received to ascertain that all return items have been examined.

CORRESPONDENT BANKS

Statements should be requested from all banks with which funds are deposited, the statements to include transactions of three to five days subsequent to the examination date. The banks should also be requested to certify the balance at the examination date. In the case of deposits with the Federal Reserve

Bank and certain other banks, daily statements are sent by them, and such statements for the period needed should be obtained from the incoming mails daily. The Federal Reserve Bank should also be asked to furnish the details of the deferred debits and deferred credits as shown by its books.

The statements of the depositories should be reconciled with the records of the bank being examined at the examination date and also the closing date of the statements received. All open items should be properly cleared (accounted for), care being taken to see that the offsetting debits and credits are made on the correct dates. The open debits appearing in the reconcilements in the client's account under the date of the examination should be compared with the schedule of outgoing mail, in addition to being cleared by seeing appropriate credits in the account of the correspondent.

If the examination is started in the morning, it will be necessary to obtain a list of the outgoing cash letters from the transit department proof. Correspondents credit the total of the items received by them subject to final payment, so that charges for return items must be reviewed to make sure that the accountant has seen the items returned. It should be ascertained that all drafts drawn to the close of business on the examination date are included in the reconcilement or have been paid. For that purpose, a schedule of the last

checks issued should be prepared at the beginning of the examination. Transfers between banks by draft and also by telephone or telegraph should be traced for the period of the latest settlement to ascertain that both sides of the transaction are properly recorded.

At some date subsequent to the date of the balance sheet a second reconciliation of all bank accounts should be made following the procedure generally outlined above.

When possible the accountant should either go to the depositary (correspondent) bank and obtain the client's statement of account, paid checks, etc., or the depositary bank should be requested to mail them directly to the accountant.

LOANS AND DISCOUNTS

The notes on hand should be listed in the classifications shown by the controlling accounts. Requests for confirmation of all loans, showing the amounts of the notes and the collateral, should be mailed to the makers.

The notes and collateral should be examined and compared with the loan department records. All collateral should be in such form that the bank may be able to realize on it, in the event it should be necessary. If warehouse receipts or real estate mortgages are held as collateral, the bank should be further protected by sufficient fire insurance. It may also be desirable to confirm ware-

house receipts with the issuers and mortgages with the mortgagors.

The collectibility of the loans should be investigated by appraisal of the collateral, reference to credit files and discussion with the loaning officers. In appraising collateral, current "last sale" or "bid" prices are used. Such pricing is not necessarily conclusive in the case of large blocks of security issues which have only a narrow market. In such cases quoted prices may need to be adjusted downward. Mortgages should be supported by current appraisals made by the bank's real estate committee or independent appraisers. Current cash surrender values of pledged life insurance policies should be obtained directly from the respective insurance companies, together with confirmation of their assignment to the bank.

The requests for confirmation should also be compared with the bank's "liability" or "line" ledger, which records the total loans to each borrower.

If the bank has a personal loan or finance division, the same procedure of proof should be followed as in the commercial loan division. Because of the volume of such loans, it may be considered advisable to request confirmation of only a portion of the loans. Some banks credit the monthly reductions on personal loans to deposit accounts, necessitating reference to those records when preparing the requests for confirmation.

It is necessary to investigate the manner of verification by the bank

of collateral such as automobiles on dealers' floors. If it appears that the check-up made by the bank is lax, it may be advisable for the accountant to make a spot check of the cars at several dealers. The method of control over repossessions should also be investigated.

INVESTMENTS OWNED

A schedule of the bonds and stocks owned should be prepared; those securities on hand should be examined and confirmation obtained of those held outside for safekeeping, pledged to secure clearings or deposits, or for other reasons not in the present custody of the bank.

Upon commencing the examination all securities held by the bank should be sealed and kept under control until all securities, including pledged collateral and securities deposited with the bank for safe-keeping, have been accounted for and checked with the records. Considerable care should be taken when examining the securities; when inspecting bonds tests should be made to see that matured coupons have been clipped and that unmatured coupons are attached; in reviewing stock certificates it should be noted that the certificates have been issued in the name of the bank or its duly appointed nominee.

The mortgages owned should be examined, and given the same scrutiny as those pledged as collateral on loans. Unless agreed with the client that it should not be done, the

amounts of mortgages should be confirmed with the mortgagors. The report should include schedules of mortgages on which principal or interest is in default, and also delinquencies in taxes. In the event of delinquencies in mortgages guaranteed by the Federal Housing Administration, it should be ascertained that notification is given the Federal Housing Administration within the required time.

The "other real estate" account should be analyzed, and steps taken to determine so far as possible that the bank is protected by insurance against the usual risks. It should be ascertained that all taxes are paid and that there are no liens against the properties. If the account includes credits representing instalment payments made by purchasers, the book amounts of the properties sold and the related credits should be stated separately in the balance sheet.

ACCRUED INTEREST

Accrued interest receivable on loans and investments should be computed or the method of accrual investigated. These accounts should include only current items.

OTHER ASSETS

The bank building account and furniture and fixtures account should be investigated. The accounts for any other assets not included in the groups already considered should be examined and, if necessary, confirmation obtained by direct correspondence.

Liabilities

CUSTOMERS' DEPOSIT ACCOUNTS

Trial balances should be prepared of the various classes of deposits. Overdrafts should be scheduled and followed up to ascertain whether or not they have been collected. Requests for confirmation of their accounts should be mailed to depositors, unless it is distinctly understood with the directors' examining committee that such confirmation is not to be included in the scope of the examination. In such event the omission of confirmation should be explicitly mentioned in the accountant's report.

A good check may be had on savings accounts by stationing an assistant at the bookkeeper's window for a certain period of time for the purpose of comparing the pass books presented for the entry of interest at interest periods or for deposits and withdrawals with the corresponding accounts in the deposit ledgers.

Certificates of deposit, cashier's or treasurer's checks, dividend checks, etc., should be reconciled by examination of the paid certificates or checks and listing of the open items. Checks drawn to the order of the bank, or its officers or employees, should be investigated, and the source of the funds used to pay for the larger checks should be traced. The schedules of outstanding certificates and checks should be used toward the end of the examination for comparing the items paid after the ex-

amination date with the corresponding record as a further proof of their correctness.

All accrued liabilities, such as interest on time deposits, taxes, etc., should be investigated and tested as to their accuracy.

Capital and Reserves

CAPITAL STOCK

The capital stock outstanding should be accounted for by examining the canceled certificates and by listing the outstanding certificates as indicated by the stubs. Confirmation of the capital stock should also be obtained from the registrar, if the stock be registered by another institution. A trial balance of the capital stock ledger should also be prepared, if the bank has not appointed another institution as transfer agent.

SURPLUS

A careful analysis should be made of the surplus account with particular attention to the charges and credits during the period under review. Amounts transferred from the undivided profits account to the surplus account should be properly approved by the board of directors, and be in accordance with provisions of law, because various states have different requirements in this connection.

RESERVES

The accountant should pay particular attention to the adequacy of the reserves for bad or doubtful loans or other accounts, allowances for de-

preciation, and other necessary valuation reserves.

Most banks are compelled to carry a reserve of some kind against their deposits, and other reserves are sometimes required by law. The auditor should familiarize himself with the requirements of the law governing the bank he is examining and determine whether the reserves carried by the bank are in accordance with the requirements.

Foreign Exchange Department

Balances due from foreign banks should be reconciled with statements obtained from the correspondents. Balances due to foreign banks should be confirmed. Future exchange contracts bought and sold should be verified by correspondence with the buyers and sellers, and a comparison made of the contract values with the values at current rates of exchange.

Letters of Credit, Acceptances, etc.

Customers' liability and the bank's liability under letters of credit and acceptances should be scheduled, and customers circularized for confirmation of their liability. The numerical sequence of both commercial and travelers' letters of credit should be accounted for. Examination should also be made of trust receipts on hand to support acceptances, and of warehouse receipts and related fire insurance policies for merchandise placed in warehouses by the bank. Guarantees of letters of credit should be examined, and charges made against

the accounts of travelers' letters of credit sold should be tested by examination of the paid drafts drawn against a number of credits.

If the bank holds for sale travelers' checks or letters of credit which are issued by other bankers, they should be verified by examination and confirmation of the correctness thereof by the issuing bankers.

Statement of Income

The furnishing of an income statement requires that sufficient investigation be made to be satisfied that the earnings are correctly stated. Tests of the collection of interest on notes, bonds owned and mortgages and of other income should be made, the extent of the tests depending on the internal check and the functioning of the internal audit department, if any. Tests should also be made of the expenses, and the interest expense should be checked by computing the interest at the applicable rates on the average balance of time or savings deposits. Unless fully covered by internal audit control, transactions in the bond account should be checked as to purchases and sales and profits and losses.

The fidelity bond and evidence of payment of the premium should be examined and consideration given to the sufficiency of the coverage.

Corporate Minutes

The minutes of the board of directors and of the executive committee should be read and pertinent informa-

tion extracted and followed through to the related entries in the records. It is advisable to ask for the latest reports made by supervisory authorities as their comments often have great value.

Trust Department

The examination of the individual and corporate trust departments should begin at the same time as that of the banking department inasmuch as certain accounts are interlocking and assets of one department may be lodged with another.

In the individual trust department, trial balances should be prepared of the trust funds applicable to the various controlling accounts carried in the general ledger of that department. Overdrafts in the principal or income accounts should be investigated. The cash on hand should be counted and the bank balances reconciled. It may be well to trace some of the cash transactions for several days prior to the examination date.

The trust investments should be examined and compared with the investment ledgers. Mortgages, stock certificates and registered bonds should be in the name of the decedent or trustor, the bank in its fiduciary capacity or the bank's nominee.

The abstract sheets which describe the terms of the trusts should be made the basis of a test to ascertain that the terms of the document under which the bank functions are being observed, both as to type of invest-

ment and the disbursing of principal and income.

Tests should be made of the accounting for income collected from trust assets, of the expenses charged to the estates, and of the commissions earned by, and expenses of, the department.

If annual examinations of the bank are made, it is well to trace a selected number of estates from their inceptions at each examination, unless the internal audit department is considered to cover thoroughly changes in corpus.

Some trust departments have mortgage pools or common trust funds which must be examined in conjunction with the other accounts examined. In such instances, the individual trust accounts carry as assets their participations in such mortgage pools or common trust funds, and it must be ascertained that the records of the pools or funds reflect the total participations as carried in the trust accounts. The accountant should familiarize himself with the terms of the indenture of the common trust fund to ascertain that they are being observed.

It is to be borne in mind that failure of a fiduciary to follow the terms of the instrument under which he functions may make him the subject of a surcharge.

Consideration should be given to requesting confirmation of the correctness of the agency and attorney-in-fact accounts, and it should be de-

termined whether or not statements of trust accounts are mailed at regular intervals.

The minutes of the trust committee should be read and determination made that the actions authorized by the committee are carried out and its instructions followed.

A trial balance of the corporate trust ledger should be prepared. Requests for confirmation of the accounts of all corporate trusteeships should be mailed to the various corporations. When the bank acts as trustee under a bond issue, any unissued bonds on hand (both certified and uncertified) should be examined; canceled bonds or cremation certificates evidencing their destruction should also be examined.

The accountant should place the paid coupons under control pending the preparation of statements and requests for confirmation, which should be mailed to the various corporations together with the paid coupons. In the smaller banks, the coupon account of each corporation is sometimes carried as a continuous account regardless of the coupon due dates. It should be recommended that separate accounts be opened for each coupon due date.

The extent of the internal check and control should be considered in connection with the examination of stock transfer accounts. In small trust companies with but few such accounts, they can be reconciled in a short time, but in the larger com-

(Continued on Page 27)

The Presentation of Financial Statements

By HERMON F. BELL

The subject of this article is the presentation of financial and operating statements, not, as most often discussed, in accordance with sound accounting principles or with painstaking care as respects the correctness or the completeness of the facts stated or the judgment used in passing thereupon, but as respects what we may call, for want of a better term, their artistic form.

Statements are sometimes recast into popular, as distinguished from technical, language, or issued in streamlined form, or variously elaborated or condensed, to meet special purposes. It is not with such procedures that we are here concerned. Rather we wish to discuss briefly, or present for consideration, the thesis that simplicity of outline, unity, correlation, proportion, and balance (in an artistic rather than in a mathematical sense) are all too often absent in smaller or greater degree from financial and operating statements as presented. Such characteristics are, however, highly desirable and worthy of greater care and consideration than they appear at times to receive.

Over the years, perhaps most markedly in recent times, accountants have had placed upon them one responsibility after another. Extreme care in factual presentation and explanations, and increasing emphasis upon

scope of audits and procedures, as well as ever greater and greater attention to fundamental principles, necessarily engage our thought. Does our thesis mean that it is now asked that the accountant be an artist as well?

I have been impressed, as I have reviewed published reports, with how greatly they vary as respects what I am pleased in this article to refer to as canons of good presentation. I have purposely confined the study as outlined herein to published reports signed by other accountants. While specific examples are not used, a few illustrations with fictitious captions and figures are included to show how presentations are sometimes made.

Both because of the nature of the subject and from choice, the purpose of this paper is not to try to state or to formulate rules or even to speak with positiveness as to how statements should be drawn up. Naturally enough, opinions or judgments will differ as to details, but it seems not unreasonable to expect general agreement as respects certain ideals of presentation.

VARIATIONS IN FORM

A striking impression gained from the review of published statements is the marked differences in form even where reported upon by the same ac-

counting firms, and for clients in the same or similar lines of business. It is scarcely an exaggeration to say that it seems at times as if almost all degrees of excellence or lack of it can be found in statements reported upon by the same accounting firm. The impression received is that the same attention and care is not always being given to the form of statements as presumably is given to audit procedures and accounting principles.

It is not for a moment intended to imply that attention should be given to form rather than to content. But on the other hand there is no conflict between accuracy of statement and good form of presentation. The former deserves the latter.

Most of us remember one or more teachers of our earlier years who, by reason of ability, enthusiasm, or outstanding personal qualities, stood out. One such comes to mind, in the field of mathematics, who was always emphasizing three requisites of good work. Always first and foremost was accuracy, correctness. Without this nothing else mattered. But given this first requisite, there were then always to be considered speed and form. It seems to me that sometimes one and sometimes the other of these last two qualities takes precedence. In detailed audit work, such as in working papers, at times speed has the call over form. But at other times, and especially in the presentation of statements, form clearly has precedence over speed.

EFFECTIVE PRESENTATION

The client is rightly charged with primary responsibility for the contents of statements. It is his task to see that his statements are good statements, that is that they reflect sound financial position and sound relations between the various assets and liabilities, and satisfactory operating results. The accountant is not responsible for the facts that are to be presented. He is concerned with accurate presentation of the facts as to present condition and the results of past operations. But is it not also the case that the form,—the unity, simplicity, correlation, proportion and balance with which the facts are stated,—enhances or detracts from the presentation? In any event good form is desirable in itself.

As accountants we are always emphasizing that our reports are not certifications but expressions of opinion, of judgment. Although the statements are statements of the client, are not the accountants who report thereon properly concerned not only with the substance of the statements but with their form, with the impression they are likely to make? Besides, if the statements are carelessly set up, without proportion and proper grouping of the elements, while it may not be so, is there not some measure of justification on the part of the reader for the thought, even though not expressed, that perhaps the audit itself was carried on with less care than should have been exercised?

Necessarily in a brief article like this there is not space for numerous illustrations. All that is attempted is to direct attention to a few considerations, and to some rules or procedures that seem desirable.

Grouping of similar items helps to bring about a desirable correlation, at once simplifying the statement and giving a better sense of perspective and proportion.

Current assets:

Cash on demand deposit and on hand.....	\$ 682,794.29
Customers' accounts and notes receivable:	
Regular, less reserve of \$60,000.....	1,643,861.40
Instalment, less reserve of \$178,315.....	1,786,314.82
Loans to employees.....	7,025.00
Sundry debtors	48,696.40
Inventories:	
Merchandise on hand, at the lower of cost or market.....	2,841,976.50
Merchandise in transit, at cost.....	97,502.65
	<hr/>
	\$7,108,171.06

Current liabilities:

Accounts payable:	
Trade creditors	\$ 1,824,861.13
Trade creditors for merchandise in transit.....	68,100.05
Accrued expenses:	
Salaries, wages and commissions.....	300,162.74
Taxes	781,426.47
Interest	189,090.42
Miscellaneous	96,021.43
	<hr/>
	\$3,259,662.24

Current assets:

Cash on demand deposit and on hand.....	\$ 682,794.29
Accounts and notes receivable:	
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Customers', instalment, less reserve of \$178,315.....	1,786,314.82
	<hr/>
Loans to employees.....	3,430,176.22
Sundry debtors	7,025.00
	<hr/>
Inventories:	
Merchandise on hand, at the lower of cost or market	2,841,976.50
Merchandise in transit, at cost.....	97,502.65
	<hr/>
	\$7,108,171.06

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Trade creditors for merchandise in transit.....	68,100.05

Accrued expenses:

Salaries, wages and commissions.....	300,162.74
Taxes	781,426.47
Interest	189,090.42
Miscellaneous	96,021.43
	<u>1,366,701.06</u>
	<u>\$3,259,662.24</u>

SURPLUS ACCOUNT ILLUSTRATION

It seems like good procedure in the surplus account to deduct dividends, as a distribution, quite apart from

any other deductions or adjustments. Rather often this clear cut separation of dividends from other deductions is not made, for example:

Earned surplus:

Balance, beginning of period.....	\$1,662,841.50
Add:	
Net profit for year.....	2,684,156.87
Excess of reserve for taxes over requirements.....	25,461.25
	<u>\$4,372,459.62</u>

Deduct:

Dividends on:

Preferred stock	\$ 425,000.00
Common stock	862,787.50
Adjustment of depreciation, applicable to prior periods.....	82,500.00
	<u>\$1,370,287.50</u>

Balance, end of period.....	<u>\$3,002,172.12</u>
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The following is a suggested revision:

Earned surplus:

Balance, beginning of period.....	\$1,662,841.50
Deduct, Adjustments applicable to prior periods:	

Adjustment of depreciation.....	\$82,500.00
Less, Excess of reserve for taxes over requirements	25,461.25
	<u>57,038.75</u>

Net profit for year.....	<u>1,605,802.75</u>
	<u>2,684,156.87</u>

4,289,959.62

Deduct, Dividends:

On preferred stock.....	425,000.00
On common stock.....	862,787.50

Balance, end of period.....	<u>\$3,002,172.12</u>
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INCOME STATEMENT ILLUSTRATION

In income statements clarity is often lacking, through failure to show such information as an intelligent reader wishes, such as gross profit or gross margin before expenses, operating expenses in total or in a few well chosen subdivisions, and perhaps also operating profit before depreciation and interest. A review of statements of income discloses, in many instances, considerable room for improvement in the grouping of items,

so that the ordinary operating results and special or more or less unusual items are clearly separated, and results shown both before and after such items. It seems sound procedure ordinarily to show operating results before income taxes, and then provision for such taxes as a distinct and separate deduction therefrom. This may seem so obvious as not to call for mention. But it is not difficult to find statements where this procedure is not followed. Example follows:

Net income from operations before depreciation, interest and provision for federal income tax.....	\$1,288,805.15
Deduct :	
Depreciation	\$399,672.18
Interest	92,746.25
Provision for federal income tax.....	140,000.00
Net income for year.....	<u>632,418.43</u>
	\$ 656,386.72

Most readers would like to see a figure representing net income before federal tax provision.

Clear cut division between income and surplus seems desirable, even where income and surplus accounts are combined in a single statement. Good form would seem to call for clear presentation on the one hand of results for the period, and on the other of change in net assets, exclusive of capital.

PERSPECTIVE AND PROPORTION

Statements are sometimes seen which show lack of perspective or proportion. Some large and important elements are stated in very condensed form, with an extreme lack of

detail, while some relatively insignificant items are given undue prominence, or are stated in unnecessary detail. In income statements especially are such alternations between the extremely important and the relatively insignificant often found. On balance sheets, deferred charges, to be spread over a long period of years, such as unamortized bond discount or other financing expense, may be found grouped with current prepaid items such as next month's rent or taxes.

RESERVES

The presentation of reserves on balance sheets is varied. Occasionally, there will be a caption, reserves,

under which appear all sorts of reserves, some that clearly should be included among current liabilities, partaking more of the nature of accruals than reserves, while others represent contingent items, and still others are practically segregations of surplus. In one instance I saw a balance sheet where a large inventory reserve followed earned surplus and was added in as part of the total of capital and surplus.

FOOTNOTES

In the past few years there has been a marked increase in the use of footnotes on statements, due in part to the influence of preparing statements for filing with the Securities and Exchange Commission. While the use of such footnotes seems likely to continue and perhaps increase, this puts a new problem before the accountant who is striving for perfection of form. Such notes can and should be so keyed into the various elements of the statements as to be correlated therewith, and be truly enlightening. They should not be just a medium for discursive explanations which might in part be avoided by greater care in the statements themselves. Obviously, it is desirable to have the elements of the statements themselves self sufficient as far as may be, and where possible to obtain clarity through sharply outlined divisions and groupings, and absence of all unnecessary explanations and qualifications, although never at the expense of accuracy.

COMPARATIVE STATEMENTS

A recent Accounting Research Bulletin, of the American Institute of Accountants, recommends increased use of comparative statements. With that recommendation there should be unanimous agreement. Although there is no sound reason why it should be so, presentation in comparative form appears from published statements often to have had an adverse effect upon the set-up, with too great condensation and lack of appropriate groupings.

There is no reason why the highly desirable increased use of comparative statements should not be accompanied by greater attention to good presentation. In fact, a challenge is now given to the accountant to exercise a considerable degree of artistic skill in setting up comparative statements in accordance with the canons of good presentation. While it is admittedly more difficult, as respects form, to present comparative than noncomparative statements, there is now an increased field in which to exercise one's talents,—and the possibility of even better presentation than in the noncomparative form.

It may seem at first glance that many of the comments in this article relate to trifles, but it is still true that, as Michael Angelo is said to have so well expressed it, "Trifles make perfection, but perfection is no trifle."

New England Conference on Taxation

BY E. E. WAKEFIELD
(Boston Office)

The Twenty-Eighth Annual Conference on Taxation under the auspices of the New England State Tax Officials Association was held at the Mountain View House, Whitefield, New Hampshire, on October 16, 17 and 18, 1940.

As was to be expected at this time, the discussions at the conference centered largely around the effect of the defense program on the finances and systems of taxation of the states.

The views expressed by the speakers were decidedly pessimistic as to the opportunities of the states for satisfactory handling of revenues and expenses in the next few years. Hardly any one was hopeful that "equity" in taxation, whatever that should mean, can be given much consideration until the paramount needs of the country for defense, and possibly for war, are met.

FEDERAL TAXES

Until about the time of the first World War, the federal government got along reasonably well with revenue from two main sources, viz., the tariff and internal revenue taxes on spirits and tobacco. However, the greatly increased demands for revenue during and since the World War have caused the federal government to encroach very widely upon the fields of taxation previously al-

lowed to the states. Increased income taxes, estate taxes, various excises on commodities and special corporation taxes have been instituted by the federal government, and apparently will be continuously used by it for an indefinite future.

STATE TAXES

Of the common forms of taxation the states have left at the present time, for their exclusive use, not much else than the general property tax and the sales tax, either generally or of partial application. That the states will continue to have the use of the sales tax, except in addition to a federal sales tax, is by no means certain. Consequently, the states are probably faced with curtailment of expenditures to as great an extent as possible and increases of rates of their existing taxes, except that those which, like Massachusetts, have not yet adopted a sales tax, may be forced to do so. Of course, the greater employment under the defense program should reduce relief and special work demands on the states, which may help them to reduce expenses.

NEW TAX SYSTEM

The present plight of the states raises the question as to whether ultimately, even if not in the immediate future, some entirely new tax system

for the country will not have to be adopted. The ways of meeting the situation discussed at the conference are as follows:

The first method considered was the abandonment of the states as revenue-raising units and, practically, the abandonment of the whole federated structure of the government of the country. Under such a plan the states would become only administrative units of the federal government without control over the raising or spending of public monies. It would hardly seem likely that so radical a change will come about in the near future, unless, through war, the country should be forced into a wholly centralized form of administration of its affairs.

A second method considered was the so-called "separation of sources" of revenue. Adoption of this procedure would mean, to some extent, a return to conditions existing before the World War, because the federal government would have to give up various taxes and sources of revenue, which it has taken over, in order to leave entirely to the states such sources as the general property tax, the estate and inheritance taxes and various excises, such as the gasoline tax. No one at the conference was ready to suggest any probability that the federal government would in the near future give up sources of revenue now available to it, so that separation of sources does not seem to be a likely solution of the present

difficulties resulting from the overlapping of state and federal taxes.

A third method of procedure discussed was an arrangement by which taxes should be levied and collected by the federal government but shared, under provisions of law, with the states. For example, the federal government might collect all the income taxes on corporations and out of the money so received allocate, as required by law, a portion to each of the states. There would, of course, be great difficulties in determining the basis on which to divide among the states, whether by population or by relative wealth of the states. Furthermore, there would very likely be endless squabbles between the states and the federal government. In theory this method of overcoming the difficulties of raising revenue as between the states and the federal government is excellent because it would simplify the whole procedure and greatly reduce the expense of raising revenue. In practice, however, no one expects that it is likely to be adopted in the near future.

A fourth method considered was the enlargement of the present procedure under which grants for special purposes as, for example, education and roads, are made by the federal government to the states, thereby enabling the states in many cases to finance expenses which they are unable to finance directly. This method of procedure again means abandonment of control by the states because, if gifts are made by the

federal government with conditions attached to them, as in the case of the social security laws, the states are unable to get the benefit of the gifts except by submitting to the domination of the federal government and its bureaus.

Altogether, none of the methods of solution of the problem being likely to be availed of or acceptable at present, it appears that the states will have to struggle along in the present more or less haphazard fashion with consequent interference with the federal government. Nobody knows what the ultimate answer will be.

INFLATION, DEBT AND TAXATION

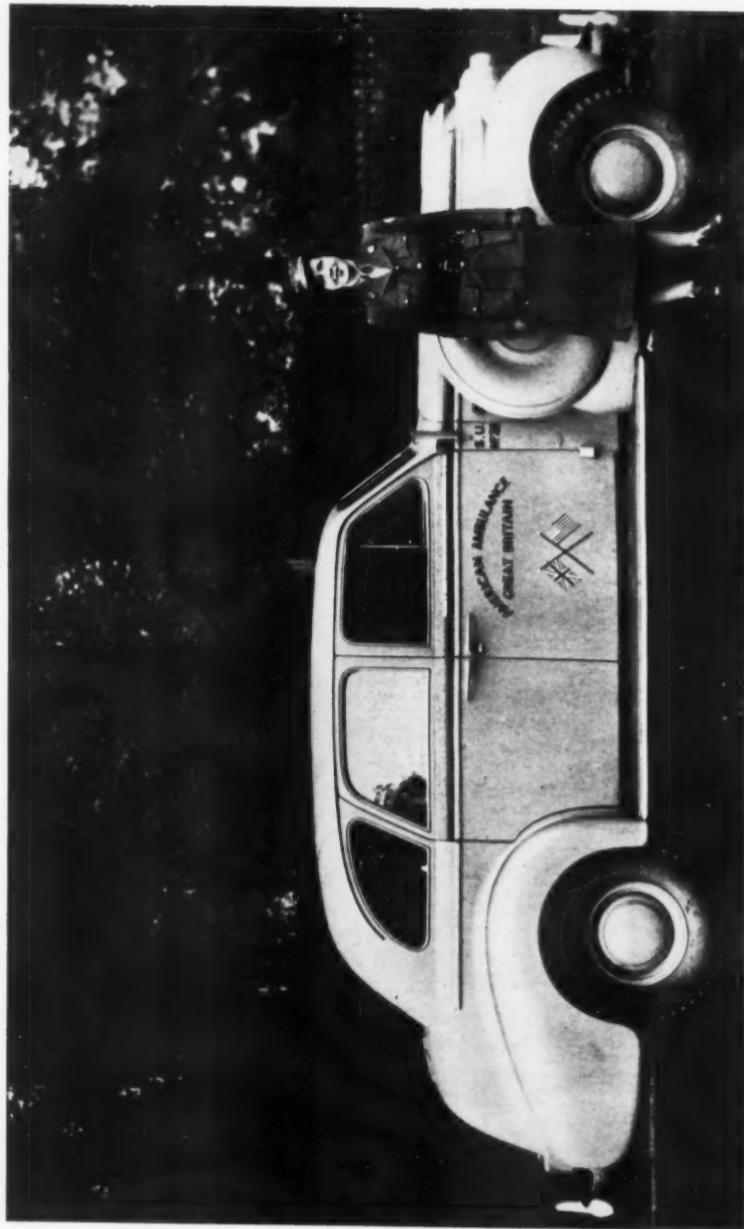
Another topic considered at the conference was the possibility of inflation and its relation to the public debt and federal and state tax systems.

Conditions in this country at present are distinctly different from those in Germany, for example, when inflation was prevalent some years ago, because we have at present a large amount of unemployed capital and labor which may be absorbed for some years by defense activity with possibly a normal relation maintained between income and cost of living, even if there is an inflationary rise in prices. The danger was pointed out, however, that proper relation between costs of living and commodities, and wages and income, cannot be maintained with wages tending to lag behind and consequent disproportion in purchasing power and the cost

of commodities. It was suggested that it may be necessary in this country, as it already is in Great Britain, in effect, to force the keeping down of prices by requiring any surplus income of all classes to be invested in government securities, thus limiting the amount that can be spent on consumers' goods and so preventing a runaway demand, with inflationary prices.

The effect of the increasing public debt was considered uncertain with possibilities of its proving either inflationary or deflationary, depending upon the trend of affairs of the country, as to which no one has any present assurance. The greatly increased deposits in banks may tend to borrowing for business expansion which will lead to inflation. On the other hand, if reasonable control can be maintained as to interest rates and the demand for government securities, it is conceivable that we may work through to the period after the defense or war period without destructive inflation or deflation. This can, in the opinion of various speakers at the conference, more likely be accomplished if the people are willing to submit to much heavier taxes spread through all the strata of the population so that borrowing may not rise too rapidly to destructive proportions. Little confidence was expressed, however, that it will be possible to avoid a ruinous depression when defense spending ceases to be heavy.

(Continued on Page 27)



AMBULANCE (SURGICAL CAR, S.U. 28) DONATED BY L. R. B. & M. TO THE FIELD SERVICE IN GREAT BRITAIN

The L. R. B. & M. Journal

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The purpose of this journal is to communicate to every member of the staff and office plans and accomplishments of the firm; to provide a medium for the exchange of suggestions and ideas for improvement; to encourage and maintain a proper spirit of cooperation and interest, and to help in the solution of common problems.

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The Forgotten Goal

One of the discouraging aspects of the present outlook for the fiscal program of our federal government during the next few years is the apparent lack of interest on the part of either the executive or the legislative departments of the government in cutting down non-essential expenditures. There has been an insidious sapping of fiscal morale in the fed-

eral government during the past eight years: first, the federal deficit was regarded as a temporary phenomenon due to the depression; then, for a period of years, there was prophecy year after year of eventual budget balancing; later, a defeatist attitude was adopted and the unbalanced budget was tacitly accepted as an unavoidable evil, and not even regarded as an evil but justified with

various sophistries; now, we are facing the necessity of staggering amounts to be expended for defense purposes, accompanied by an unwillingness to effect any considerable reduction in non-defense expenditures.

A common sense viewpoint of this situation would be that, in view of the tremendous stimulus to industry—even if for the long pull a basically unsound one—which must result from the emergency expenditures, the time had come when a considerable reduction could be affected in those expenditures which had contributed so greatly to the unbalancing of the national budget during the past eight years. Various business organizations were not slow to point to this opportunity and, even more, the necessity to do so.

For example, the New York Merchants Association, of whose Taxation Committee Mr. Staub is a member, made a vigorous recommendation during the consideration of the excess profits tax bill last Summer that a drastic cut be made in the expenditures of the regular budget so as to offset in part at least the tremendous outlay in prospect for defense measures. The National Economy League, of whose Executive Committee Mr. Keller is a member, has been issuing a series of informing reports which contain important recommendations along the same line. Several years ago when those who were advocating the balancing of the budget were challenged to submit concrete plans to accomplish that purpose, the

League submitted definite suggestions to do so over a period of several years. Unfortunately, neither Congress nor the President appear to have given that report serious consideration.

In the League's report of December 30, 1940, which has been published under the title of *Indefensible Spending*, it submitted carefully reasoned proposals for savings in non-defense expenditures aggregating \$394,000,000 for the six months, January-June, 1941, and \$2,043,000,-000 for the government's fiscal year ending June 30, 1942. The proposals of the League derive added authority from the fact that they have the concurrence of Professor Harley L. Lutz, of Princeton University, who is Consulting Economist of the League.

The following summary and conclusions which appear in the report indicate how important are the League's recommendations:

With the defense program demanding the utmost use of our financial and economic resources, the country cannot afford to support programs which were luxurious even before the defense emergency was recognized. Congress and the administration must now have the courage to reduce every expenditure not required for defense or essential government.

The magnitude of the defense appropriations themselves calls for extraordinarily efficient management, and Congress should be on guard against the masquerading of pet projects under the defense label.

The following considerations demonstrate the compelling need for present reductions in non-mandatory expenditures:

1. The support of our defense establish-

ment will require sacrifices beyond the present realization of most taxpayers. The burden can be met only if defense costs are offset to the greatest possible degree by economies elsewhere in the budget.

2. Rising employment in defense industries, with secondary effects on consumer goods industries, including agriculture, will sharply decrease the need for public assistance to distressed sections of the population.

3. Continuation of subsidy programs in the face of huge defense expenditures would intensify the upward pressure on prices and impose an unjustified burden on persons with fixed or lagging incomes. The principal task of economic leadership in the near future is the reverse of pump-priming. The coming "prosperity" must be kept in hand, not only to prevent disastrous confusion in defense production but to facilitate the transfer to peacetime activity without large federal deficits in the future.

4. Public works and work relief projects compete directly with defense production in the markets for construction labor and materials. Stimulation of consumption competes indirectly for productive resources and increases the cost of defense materials to the government.

The economics recommended in this study are drastic—\$394 million in the remaining six months of the present fiscal year and \$2,043 million in the 1942 fiscal year—but the necessity for a tapering-off period is recognized, and provision is made for continuing moderate programs of relief and agricultural aid to prevent hardship. The savings can be made if the administration and Congress have the determination to do so, and if minority groups are willing to forego special advantages for the national good.

Accounting Conscious

In previous issues of the JOURNAL the writer has occasionally called at-

tention to the extent to which accounting and accountants are the subject of reference in that figurative way that helps to "get over" a thought which one is endeavoring to express.

In an editorial in the *New York Sun*, entitled "The Rear Guard," which expressed admiration for the splendid work the Allies did in extricating the army which was left at a tremendous disadvantage when the Belgians capitulated, the writer used the following expression:

It is perhaps natural that attacking airmen—who at best must proceed at high speed, *without time to tarry and make up a balance sheet that would pass an auditor's inspection*—should give themselves full credit for what they think they have accomplished as well as for what they actually have accomplished. (Italics supplied.)

The following, which appeared in a recent issue of the *Newark Evening News*, is another indication of the recognition of the importance of accounting in the present day:

Farm Accounts

One of the most important practices on the farm, if not the most important, is the keeping of accounts. Determining the value of the farm's possessions at the beginning of a new year, a record of the receipts and expenditures throughout the year and an analysis of results at the end of the year, are the only means of determining profitable operations from those carried along at a loss.

With agricultural problems an increasing factor and economic production a matter of concern, knowing where the monies come from and their ultimate distribution are important. Even more, a necessity to success.

There are simple systems of farm accounts, requiring only a few minutes' time daily for their use. Employ them and thereby protect the farm's future.

Opportunities in America

A book of recollections by George W. Childs, written in 1890, contains an account of the welcome given to General Grant upon his return from his trip around the world after the completion of his two terms as President of the United States.

General Grant was gone for over two years on this trip and visited every capital in Europe and most of the Eastern nations. In the course of his remarks at the welcome given him by the Grand Army of the Republic in Philadelphia on his return home, he said, among other things, the following:

Comrades, having been compelled, as often as I have been since my arrival in San Francisco, to utter a few words not only to ex-soldiers, but to all other classes of citizens of our great country, and always speaking without any preparation, I have necessarily been obliged to repeat, possibly in not the same words, but the same ideas. But the one thing I want to impress on you is that we have a country to be proud of, to fight for and die for if necessary. While many of the countries of Europe give practical protection and freedom to the citizen, yet there is no European country that compares in its resources with our own. There is no country where the energetic man can, by

his own labor, and by his own industry, ingenuity, and frugality, acquire competency as he can in America.

A trip abroad, and a study of the institutions and difficulties of a poor man making his way in the world, is all that is necessary to make us better citizens and happier with our lot here.

Although these words were spoken some sixty years ago, the substance of them seems just as true as the day the conviction was expressed by General Grant concerning the opportunities offered in America.

A short time ago, Charles B. Seger, formerly president of the Union Pacific Railroad Company and of the United States Rubber Company, passed away. His life was a testimony to the truth of the above quoted remarks of General Grant. Seventy-three years ago he was born in New Orleans, there he began his career as an office boy with Morgan's Louisiana & Texas Railway & Steamship Company, a part of the Southern Pacific Railway. He worked his way up to general auditor, then through one position and another to auditor of the Union Pacific System, later vice-president and comptroller, and still later president of the Union Pacific.

Opportunities are still to be found in America by those who seek them and who are willing to put in the physical and mental effort necessary to measure up to them.

Notes

John Kenneth Mathieson, immediate past president of the American Institute of Accountants, passed away on January 10 at the age of 48 years. Although he had not been in the best of health during the past year, the news of his demise was nevertheless a shock to his friends. The news was heard with especial regret by our firm for he was an L. R. B. & M. alumnus.

He began his training in the field of public accounting in our Philadelphia office in 1912, and continued his work there until May, 1917, when he received a commission in the U. S. Army and entered upon war service. After the conclusion of the World War he returned to our Philadelphia office. Some time thereafter he left us to join the firm of which he eventually became the senior partner.

"Ken" Mathieson always enjoyed the high regard of all those who knew him. The esteem of his fellows, and the appreciation felt for his activities in the interest of the profession at large, were evidenced by his election to the highest position in the gift of the profession, namely, the presidency of the Institute.

Appointments of members of our firm and of other members of the L. R. B. & M. organization to serve on committees of the American Institute of Accountants during the

current Institute year have been announced as follows:

MR. ROSS:

Committee on education (Chairman)

COLONEL MONTGOMERY:

Executive committee

MR. STAUB:

Committee on accounting procedure

MR. DUMBRILLE:

Special committee on stock brokerage accounting

MR. SWEET:

Special committee on cooperation with Securities and Exchange Commission (Chairman)

MR. SINCLAIR:

Special committee on cooperation with stock exchanges

Special committee on national defense

MR. SCHAFFER:

Committee on auditing procedure

MR. FISCHER:

Committee on professional ethics

MR. A. E. HUNTER (Boston):

Nominations committee

MR. T. W. MOHLE (Houston):

Special committee on accounting for state highway departments (Chairman)

In addition, Colonel Montgomery is an ex-officio member and Mr. Fischer an elected member of the Council, and Mr. Hunter is president of the Advisory Council of State Society Presidents.

Mr. Staub was one of a large number of citizens, headed by Mr. Thomas J. Watson (President of International Business Machines Cor-

poration) as Chairman, who gave a luncheon in honor of Mr. Henry W. Taft who has served more than twenty years as Chairman of the Advisory Council of The Salvation Army, as well as having given untiring service to many other charitable and community efforts. The luncheon was held at the Waldorf-Astoria Hotel on January 7, the toastmaster being Mr. Walter Hoving, President of Lord & Taylor. Mr. Hoving is President of The Salvation Army Association of New York and has rendered service of marked value to The Army in his Chairmanship of the Annual Campaign for some years past. Mr. Lybrand, Mr. Bell and Mr. Staub were present at the luncheon.

The address on "Provisions in Defense Contracts," which Mr. Perry delivered at the New England Regional Conference of the National Association of Cost Accountants last fall, was published in Section I of the November 1, 1940 issue of the *N. A. C. A. Bulletin*.

Mr. Arthur P. Caldwell, Jr., who was a member of our New York staff for quite a number of years, and who has been a junior officer of the Chemical Bank & Trust Company for some years has recently become a vice-president of that outstanding bank. We congratulate Mr. Caldwell on this fine recognition of his ability and integrity.

The paper on "Inventories of Nonferrous Metal Mines, Smelters and Refiners," which Mr. Edward G. Carson, of our New York staff, presented at the special technical meeting held on April 17, 1940, under the direction of the Committee on Mining and Smelting Accounting of the New York State Society of Certified Public Accountants, was published in the January, 1941, issue of *The New York Certified Public Accountant*. Mr. Carson has had considerable experience with accounting in the nonferrous metals industry and is a member of the Society's Committee on Mining and Smelting Accounting.

The October, 1940, issue of *The New York Certified Public Accountant* contained an article by Mr. Raymond L. Collett, of our New York staff, on "Electrical Operation of Card Files."

Messrs. Edward H. Anzalone and Gilbert A. Jenkins, of our Cleveland staff, have been admitted to membership in the American Institute of Accountants.

Mr. Charles B. Peck, of our New York staff, was recently advanced from associate to membership in the New York State Society of Certified Public Accountants.

In view of the comeback of the phonograph, it has been suggested that creditors send a record to delin-

quent debtors, with the following query (set to the music of "Comin' Through the Rye" and sung slowly and with great feeling):

If a body trust a body
And fail to get prompt pay;
May a body ask a body
Please remit today?

with the suggestion, "Please try this on your phonograph!"

New England Conference on Taxation

(Continued from Page 20)

AFTER THE WAR, WHAT?

At the dinner session of the conference the speaker was Roger Babson of the Babson Statistical Organization, whose subject was "After the War, What?"

Mr. Babson predicted very great changes in both the social and the economic structures of the country. He looks to see use of the air change the life of the country much as the life of England was changed several centuries ago when it began to send its ships all over the world. He also expects great changes in our educational system, as he says that our high schools are turning out "unemployables" in great numbers and their curricula will have to be modified to provide more disciplinary training and more direct preparation for earning a living, in many cases with the hands and not exclusively with the head. He also thinks that the trend of population away from the cities

will be greatly increased, in part because of the lessons learned from the present world war and the desire to protect industry and the population of the country from the destructive bombing attacks on thickly populated cities.

The point Mr. Babson most emphasized, however, was that, as he says Thomas A. Edison told him just before Mr. Edison died, the country has to go a long way to catch up "spiritually" before it can successfully use more changes due to advance of science and on the materialistic side of living.

OTHER PROBLEMS

Other subjects discussed at the conference were recent legislation and court decisions in the New England States and New York, administrative problems in state taxation and the valuation of real estate for tax purposes as compared with loan purposes.

Bank Examinations by Public Accountants

(Continued from Page 11)

panies considerable time would be required for their verification.

Requests for Confirmation

All requests for confirmation should be mailed by the accountant in envelopes bearing his return address, and should be accompanied by return envelopes addressed to the accountant at his office. Replies to the requests

for confirmation should be submitted to the officials of the bank for the purpose of verification of signatures, after the replies have been compared with the copy of the request for confirmation in the possession of the accountant. The person verifying the signatures should not be connected with the department to which the replies pertain.

Due to the war it is increasingly difficult to obtain confirmation of accounts from customers located in foreign countries, especially in the belligerent nations. This fact requires careful consideration by the auditor of the procedures he is to use in determining the accuracy of the accounts in question.

The Accountant's Report

The accountant's report should comment on any items which for any reason it has not been possible to cover fully, as well as accounts for which requests for confirmation were not mailed. The schedules furnished usually depend on the wishes of the client but, in addition to the balance sheet and statements of undivided profits and income account, they

should include past due and under-margined loans, and any other items considered necessary for the attention or information of the client.

It is important to observe the routine and personnel of the institution for the purpose of calling to the attention of the management any weaknesses in the system or methods and for the purpose of making suggestions for improvement. A discussion with an operating officer regarding the system should not be considered to be sufficient, as clerks have been known to deviate from the prescribed routine without the knowledge of their superiors.

It is obvious that it is not feasible for a board of directors to make an examination of the scope outlined above from the time element alone, and that such an examination is broader in its scope than the examinations usually made by the regulatory bodies. For these and other reasons many banking institutions after a lapse of some years due to economic conditions are again engaging the public accountant to assist the members of the board in the discharge of their responsibilities.



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